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In the

Supreme Court of the United States

October Term, 1962

No. 970

Edward J. Brunenkant,

Petitioner

v.

Anthony J. Celebrezze, Secretary
Of Health, Education and Welfare,

Respondent

PETITION FOR A WRIT OF CERTIORARI
TO
UNITED STATES COURT OF APPEALS
For The Seventh Circuit

Edward J. Brunenkant,
Attorney Pro Se.
11641 Hacienda Drive,
Sun City, Arizona

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OPINION BELOW

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit entered in the above case on October 31, 1962. Decision of the Court is in this petition, Appendix pp. 16-23.

JURISDICTION

The judgment of the Court of Appeals for the Seventh Circuit was entered on October 31, 1962. Thereafter petition for rehearing was filed and denied on Januray 2, 1963. The jurisdiction of this Court is invoked under 28 U.S.C. #1254 (1).

QUESTIONS PRESENTED

1. Whether the salaries paid to the petitioner by the Commodity Investment Corporation for services as its president and attorney for the years 1955, 1956 and 1957 constitute "wages" for the said years under the Social Security Act?

2. Whether the income of the petitioner for the years 1955, 1956 and 1957, derived from his activity as a member of the Chicago Board of Trade and engaged as an Odd-lot Futures Specialist in wheat futures on the Exchange Floor, constituted self-employment income for the said years under the Social Security Act?

3. Whether petitioner's activity as an Odd-lot Futures Specialist for the years 1955, 1956 and 1957 constituted the business of a dealer in commodity futures so as to bring his income derived from such activity within the exclusions from capital gain income provided in the capital asset statutes and constitute it self-employment income under the Social Security Act?

STATUTES AND REGULATIONS INVOLVED

"Definition of wages:—The term "wages" means*** remuneration paid after 1950 for employment, including the cash value of all remuneration paid in any medium other than cash***." S.S.A. #209; 42 U.S.C. #409.

"Definition of employment: — The term "employment" means*** any service of whatsoever nature, performed after 1950 either (A) by an employee for the person employing

him, irrespective of the citizenship or residence of either, (1) within the United States." S.S.A. #210 (a); 42 U.S.C. #410 (a).

"Definition of American employer:—The term "American employer means an employer which is*** (6) a corporation organized under the laws of the United States or of any state." S.S.A. #210 (e); 42 U.S.C. #410 (e).

"Definition of employee: — The term "employee" means (1) any officer of a corporation." S.S.A. #210 (k); 42 U.S.C. #410 (k).

Definition of self-employment income, S.S.A. 211 (a), 42 U.S.C. #411 (a). Quoted verbatim at page 13 herein.

Definition of "capital asset", 1954 Internal Revenue Code, 26 U.S.C. #1221 (1). Relevant part at pages 13-14 herein.

Definition of "trade or business" as used in the Social Security and Revenue Acts:

> "The term, 'trade or business' when used with reference to self-employment income, shall have the same meaning as when used in Section 23 of the Internal Revenue Code." S.S.A. #211 (c), 42 U.S.C. #411 (c).

Sections 23 and 161 of the Internal Revenue Code fail to define "trade or business" or "carrying on a trade or business". This Court has noted such fact in Higgins v. Comm., 312 U.S. 212 wherein it stated:

> "No regulation has ever been promulgated which interprets the meaning of 'carrying on a business' nor any rulings approved by the Secretary of the Treasury.*** To determine whether the activities of a taxpayer are 'carrying on of a business' requires an examination of the facts in each case."

G.M.C. 19322, XV-2 Cumm. Bull. 192-5 quoted at page 10 herein.

FACTS RELATING TO THE COMMODITY INVESTMENT CORPORATION

The Commodity Investment Corporation is a duly organized and operating corporation under the laws of Illinois. Its

charter, granted on November 14, 1953, provided it with broad powers to buy and sell commodities, commodity futures, stocks and bonds, oil and mineral rights and leases and to deal in real estate or any interest therein. Its original authorized capital issue consisted of 1,000 shares of common of $1.00 par value and 10,000 shares of 8% Cumulative preferred of a par value of $100.00 per share. (R. 136-7-8-9.)[1]

The common stock was owned by the plaintiff, his wife and children. The plaintiff was the duly elected president of the corporation and his wife and daughter were also officers. (R. 225, 37, 85.)

The corporation's office and address was 2785 Prairie Avenue, Evanston, Illinois, where it shared with the plaintiff in his home a fully equipped law office with adequate telephone service. (R. 95.)

By appropriate resolution the corporation's Directors at a meeting held on November 30, 1953, employed the plaintiff as its attorney.

The major activity of the corporation during its formative years, 1954 through 1957, were concerned with its efforts to distribute its preferred stock to private investors. The necessity of qualifying such issue before the several Security Commissions and the negotiation and execution of Underwriter contracts required a considerable amount of legal effort and research extended over a prolonged period. (R. 38.)

During the years 1955, 1956 and 1957, the corporation traded in commodity futures listed on the Chicago Board of Trade. For this purpose it used its own capital of $1,000.00 and some additional borrowed capital. As president, the plaintiff directed all of the corporation's trading transactions. They were entered in the corporation's trading account with the Uhlmann Grain Company to whom the corporation paid the

1 Record references are to Administrative Records filed with the Court of Appeals.

usual customer's commission on every transaction. (R. 40, 104-5.)

There was not at any time any mingling or commingling of the transactions or accounts of the petitioner with those of Commodity.

The net earnings of Commodity from its trading operations, exclusive of the salaries paid to the plaintiff, were as follows (R. 154, 161, 285, A. p. 28):

1955	$4,500.00
1956	356.00
1957	1,827.00

Each year, by appropriate resolution, the corporation's Directors provided a salary for its president of $4,200.00 annually. (R. 132-3-4, A. p. 27.)

The corporation records show that salary payments were made in cash and promissory notes of the corporation as follows:

Year	Total Payment	Medium of Payment	Amount in Each Medium
1955	$4,200.00	Cash t D. I. Revenue	$ 624.00
		Cash to Plaintiff	3,576.00
1956	$4,200.00	Cash to D. I. Revenue	624.00
		*Notes Payable	3,576.00
1957	$4,200.00	Cash to D. I. Revenue	526.52
		*Notes Payable	3,673.48

* Notes payable, bearing interest at 4% per annum, were subsequently paid at face value plus accrued interest by the issuance therefor of 8,000 shares of the common stock of the Commodity Investment Corporation, with a par value of $1.00 per share. (R. 226-7, A. p. 29.)

The Commodity Investment Corporation withheld from the salaries payable to the petitionor his liability for income and social security taxes thereon in the amounts of $624.00 for each of the years 1955 and 1956 and $526.52 for the year 1957 and with its own liability for Federal Insurance Contribu-

tion taxes on such salaries, it paid to the Director of Internal Revenue, Chicago, the following amounts (R. 251 to 256):

1955	$708.00
1956	708.00
1957	621.00

Commodity's tax returns show salary payments as expense deductions for each of the years 1955, 1956 and 1957 in the amount of $4,200.00 After office audit by the Bureau of Internal Revenue, they were approved as filed. R. 39.)

The petitionor reported on his personal income tax returns the salaries received from the Commodity Investment Corporation in the amount of $4,200.00 for each of the years 1955, 1956 and 1957. (R. 39.)

FACTS RELATING TO PETITIONER'S ACTIVITY AS AN ODD-LOT FUTURES SPECIALIST

The Chicago Board of Trade functions both as a cash grain and futures market. Approximately one-third of its membership of 1425 are engaged as cash grain dealers with their businesses conducted either from the Exchange Floor or from grain elevators scattered over the grain producing areas.

There are two Board of Trade contracts in grain futures. One is a 5,000 bushel contract which is widely used and the other, a 1,000 bushel contract, which is little known beyond the Exchange membership. It is called an odd-lot contract and was created to supply the hedging needs of the cash grain dealers whose transactions with producers were generally made in lots of less than 5,000 bushels. To supply the hedging needs of the cash grain dealers there assembled in each grain pit a small group of members, known as odd-lot specialists, who dealt exclusively in odd-lot futures and whose trading was confined to the cash dealers since traders, speculators and investors rarely traded or were interested in the lesser 1,000 bushel contract.

The activity of the petitioner as an Odd-lot Futures Specialist required the investment of capital in a Board of Trade membership, in inventories of futures and in operating costs.

During each daily session of the Exchange, the petitioner was stationed at one end of the wheat pit on the Exchange Floor prepared to buy or sell to his cash dealer customers odd-lot wheat futures in any quantity at a price of ⅛ of a cent per bushel from the quoted round-lot, 5,000 bushel, price. Petitioner realized a gross profit of $1.25 on each completed odd-lot, 1,000 bushel, transaction.

It was part of the business process in petitioner's activity that he maintain at all times large inventories of odd-lot futures either in an inventory "short" position resulting from sales of odd-lots to his customers or in inventory "long" position resulting from purchases of odd-lots from his mustomers. It was his practice to keep his inventory in odd-lot futures, at all times during and after market sessions, completely hedged in concurrent futures. Such hedging practice resulted in inventories of both odd-lot and round-lot futures, i.e., petitioner's "long" position in odd-lots would be hedged in a corresponding "short" position in round-lots of the same future or his "short" position in odd-lots would be hedged in a "long" position of round-lots.

The effect of petitioner's hedging practice was to insure his inventories of odd-lot futures from risk of loss arising from price swings in the futures during the interim period pending inventory liquidation. At the same time, such hedging preserved his merchandising mark-up of ⅛ of a cent per bushel reflected in his inventory prices. While his inventory hedging insured petitioner against inventory price swing losses, it at the same time precluded inventory price swing profits. Its net effect was to create for petitioner a non-speculative inventory position in futures. Therefor, petitioner's earnings from his activity, depended solely upon the volume of his transactions. For the years 1954 to 1957, inclusive, his net earnings from this activity were as follows:

1954	$12,262.30
1955	5,681.00
1956	4,950.00
1957	4,545.19 (R. 106.)

Copies of the plaintiff's daily inventories for the last trading days of March and November for each of the years 1955, 1956 and 1957 are in the Administrative record. (R. 180 to 198, incl.) An examination of plaintiff's inventory of March 29, 1956 (A. pp. 35-36), shows his inventory hedged position to be as follows:

"Long" Position	"Short" Position
May Wheat Futures	
165 job-lots, 165,00 bu.	33 round-lodts, 165,00 bu.
July Wheat Futures	
15 job-lots, 15,00 bu.	3 round-lots, 15,000 bu.
September Wheat Futures	
1 round-lot, 5,000 bu.	4 job-lots, 4,000 bu.

On March 29, 1956, the plaintiff's inventory of futures consisted of 370,000 bushels with 369,000 bushels hedged and 1,000 bushels unhedged.

REASONS FOR ALLOWING THE WRIT

1. The decision of the Court of Appeals herein is in conflict with decisions of the Court of Appeals for the Ninth Circuit in Stark v. Flemming, 283 F. 2d 410 and Flemming v. Lindgren, 275 F. 2d 596. These cases hold it error for the Secretary to disregard the corporate entity in a social security case where there has been adherence to the normal corporate routines. They also hold that motivation of a wage earner to secure social security benefits through a family owned corporate set-up is not a valid defense to defeat coverage where bona fide services have been rendered to the corporation by the officer-employee.

In a per curiam decision, the Court in the Stark case reversed the District Court, which upheld the Secretary in his defense that the corporate set-up was a device and sham used to secure social security coverage for the plaintiff. Quoting from the Court's opinion:

> "But here there seems to have been proper adherence to the normal corporate routines. And it is difficult to understand how the corporate arrangement would not have to be respected by others than the Secretary. And we think he must respect it, too. * * * * * Congress could have provided that motivation to obtain social security by organizing a corporation would defeat the end. It did not."

The Ninth Circuit decisions in the aforesaid cases have been quoted with approval and followed in two recent social security decisions, — Enke v. Ribicoff, 197, F. Supp. 319 and Brannon v. Ribicoff, 200 F. Supp. 697.

2. Petitioner believes that the Court of Appeals decision is in conflict with the decision of this Court in Corn Products Refining Co. v. Comm. of I.R., 350 U.S. 46 which was relied upon by the appellant as being dispositive of the second issue as to whether his income, realized from his activity as an Odd-lot Futures Specialist, constituted self-employment income under the Social Security Act.

As an Odd-lot Futures Specialist on the Chicago Board of Trade, the petitioner maintained at all times large inventories of odd-lot wheat futures to supply the needs of his customers who were members of the Exchange operating as cash grain dealers. To protect and insure such odd-lot inventories from risk of loss arising from price swings in the futures and to preserve his gross profit mark-up of ⅛ of a cent per bushel during the interim period of inventory disposition, petitioner hedged his odd-lot futures in round lots of the same futures or, as is generally termed, in concurrent futures. Such hedges were made as simultaneous transactions with purchase or sale-

of odd-lot futures during a market session. Such practice resulted in the maintenance at all times of a 99% hedged inventory position.

The Court of Appeals in its opinion stated that petitioner's reliance on Corn Products was "misplaced" in that he was not a manufacturer, processor or handler of actuals and that his purchases and sales of futures were not perfectly matched nor made at identical prices but, were made at a differential of 1/8 of a cent per bushel.

Petitioner believes that the Court's interpretation of the Corn Products decision is incorrect; that such decision does not impose any limitation of engagement in a particular business or activity to qualify as a bona fide hedger nor does such decision indicate a requirement that in bona fide hedging the purchases and sales be perfectly matched or at identical prices.

In the Corn Products opinion, this Court stated that it had recognized for 20 years the Treasury pronouncement contained in G.C.M. 17322, XV-2 Cumm. Bull. 152-5 which distinguished speculative transactions in commodity futures from hedging transactions. It held that hedging transactions were essentially to be regarded as insurance rather than a dealing in capital assets and that gains and losses therefrom were ordinary gains and losses. Its pertinent provisions follow:

> "Where future contracts are entered into to insure against * * * risks inherent in the taxpayer's business, the hedging operation should be recognized as a legitimate form of business insurance. * * * Future contracts which are not hedges against spot transactions are speculative unless they are hedges against concurrent futures or forward sales or purchases."

This Regulation expressly recognizes hedges against concurrent futures as being non speculative even though they are not hedges against actuals, — spot transactions.

All of petitioner's hedging transactions were in concurrent futures. They were entered into for the sole purpose of in-

suring his inventories of odd-lot futures from the risk of loss arising from the price swings in the futures during the interim inventory disposition period. Such hedging practice was an integral part of his business process which assured and preserved his gross profit mark-up of 1/8 of a cent per bushel on each odd-lot transaction.

Accordingly, the Court of Appeals requirement that bona fide hedging in commodity futures be limited to a processor, manufacturer or handler of actuals is in conflict with G.C.M. 17322 and the decision of this Court in Corn Products.

The other requirements of the Court Appeals decision that in bona fide hedging the purchases and sales must be evenly matched and at identical prices are contrary to established hedging practice. In an early tax case, Stewart Silk Corporation, 9 Tax Court, 179, the Court held:

> "Petitioner makes no contention that it sought to hedge its entire market risk 100 per cent. And, we do not understand that in order to constitute a true hedge, it was necessary for petitioner to cover his entire inventory and offset every purchase of actuals with a corresponding future's contract."

The other requirement of the lower court that purchases and sales be made or matched at identical prices is an impractical limitation on bona fide hedging. When futures are hedged against actuals, the hedger rarely, if ever, is able to make his purchases of actuals and his sales of futures at identical prices. Seldom, if ever, are spot and future prices identical and generally the price spread is substantial.

3. Petitioner believes that the Appellate Court in holding that his income from his Board of Trade activity constituted capital gain income results from a broad construction given to the term, 'capital asset' which is in conflict with the rule of construction applied by this Court in Corn Products.

> Quoting from the poinion of the Appellate Court:
> "And to the extent that his future commitments remained unmatched he took the full risk of price swings. * * * the

fact that plaintiff chose contemporaneously to match most of his transactions (thereby taking only the risk of daily short swings in the market), and run the risk of long-run price fluctuations on a small part of his trading merely reveals plaintiff's conservative trading position. The limited degree of his speculation does not, for the purposes here concerned, either change the nature of his trading activities or qualify his profits therefrom as self employment income rather than capital gains."

In the petitioner's activity, his hedging in concurrent futures, or as the Court below terms it, "matching", consisted of *simultaneous* transaction made during a market session by the purchase or sale of odd-lot futures and reverse hedging transactions in round-lot futures of the same option. The time lapse between the transactions was always a matter of seconds so that substantially all risks from price swings in the futures, with respect to his hedged position, were entirely eliminated.

The Appellate Court rests decision on the fact that a small portion, approximately 1%, of petitioner's transactions were unhedged. Such fractional part of petitioner's activity was speculative but the substantial portion, 99%, which was protected from price swing risks by hedging, was non-speculative.

Under these facts, to constitute petitioner's activity income capital gain income, requires a broad construction of the capital asset statute of the Social Security Act. Such broad construction is contrary to the rule of construction applied by this Court in Corn Products to #117 of the 1939 Revenue Act, having identical provisions with the Social Security statute. Quoting from such decision:

"Congress intended that profits and losses arising from the everyday operation of a business be considered as ordinary income or loss rather than capital gain or loss. (p. 52) * * * * The preferential treatment provided by #117 applies to property which was not the normal source of business income. In was intended to relieve the taxpayer from excessive tax burdens or gains or losses resulting from a conversion of capital investments and to remove the deterrent effect of

those burdens on such conversions. Burnet v. Harmel, 287 U.S. at 106. Since this section is an exception from the normal tax requirements of the Internal Revenue Code, the definition of a capital asset must be narrowly applied and its exclusions interpreted broadly. This is necessary to effectuate the basic Congressional purpose. This Court has always construed narrowly the term "capital assets" in #117."

The third question presented herein is whether petitioner's activity as an Odd-lot Futures Specialist was engagement in the business of a dealer in commodity futures so as to bring his activity income within the statutory capital gain income exclusions of the Social Security Act and constitute self-employment income under the said Act.

The Referee decided this question adversely to petitioner. It was presented to the Appellate Court which did not mention this issue in its decision but by its affirmance of the Secretary's decision, affirmed the decision of the referee.

Section 211 (a) of the S.S. Act, 42 U.S.C. 411 (a), provides, in pertinent part:

> The term "net earnings from self-employment" means the gross income, as computed under Chapter 1 of Title 26, derived by an individual from any trade or business carried on by such individual * * *; except that in computing gross income * * *
>
> (3) There shall be excluded any gain or loss (A) which is considered under Chapter 1 of Title 26 as gain or loss from the sale or exchange of a capital asset, * * * or (C) from the sale, exchange, involuntary conversion or other disposition of property if such property is neither (i) stock in trade or other property of a kind which would properly be includible in inventory if on hand at the close of the taxable year, nor (ii) property held primarily for sale to customers in the ordinary course of the trade or business, * * *".

Section 117 (a) of the 1939 Internal Revenue Code and #1221 (1) of the 1954 Code exclude property from being

capital assets identical with the property excluded in (i) and (ii) of the Social Security statute:

> "For the purposes of this subtitle, the term 'capital asset' means property held by the taxpayer * * *, but does not include —
>
> (1) Stock in trade or the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."

Petitioner belives that his activity on the Chicago Board of Trade constituted the business of a dealer in commodity futures; that his inventories of odd-lot wheat futures were valuable property and his stock in trade acquired for the sole purpose of sale to his customers who were the cash dealer members of the Chicago Board of Trade. These facts bring petitioner's income within the express exclusions from capital gain treatment contained in the above statutes and constitute it self-employment income under the Social Security Act. The Appellate Court, in affirming the referee decision, construed the exclusions of the aforesaid capital gain statutes narrowly and in conflict with Corn Products wherein this Court favored a broad construction.

This proceeding concerns remedial statutes wherein the intention and purpose of Congress, as shown by its many amendments to the original Social Security Act, has been directed toward liberalizing its provisions and the administration thereof in favor of coverage to include additional groups and persons eligible to social security benefits.

To implement congressional intent and purpose, the courts have always favored a liberal construction in the administration and interpretation of the Act's provisions.

The Court so held in Burger v. Social Security Board, 66 F. Supp. 619-28 at page 626:

"It is well settled that the Social Security Act should be liberally construed in favor of those seeking its benefits. All doubts of interpretation are to be reseolved in favor of coverage. Helvering v. Davis, 1937, 301 U.S. 619, 640-645*** Grace v. Magruder, 1945, 80 U.S. App. D.C. 53, 148 F. 2d 679; Carroll v. Social Security Board, 7 Cir. 128. Fed. 2d 76-81.

The administrative decisions in this case have been arbitrary to the extent of ignoring record facts and substituting therefor abstract facts to support factual findings. There was here concurrence in sueh action by the appellate Court in affirming the Secretary's decision. Accordingly, the Appellate Court's decision in conflict with the foregoing rule of liberal construction of the provisions of the Social Security Act in favor of one seeking its benefits.

CONCLUSION

For the reasons set forth herein, it is respectfully submitted that the petition for a writ of certiorari be granted.

EDWARD J. BRUNENKANT,
Attorney Pro Se.

APPENDIX

In the

United States Court of Appeals

For the Seventh Circuit

No. 13715 SEPTEMBER TERM, 1962
SEPTEMBER SESSION, 1962

EDWARD J. BRUNENKANT,
Plaintiff-Appellant,
v.
ANTHONY J. CELEBREZZE, Secretary of Health, Education and Welfare,
Defendant-Appellee.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

October 31, 1962.

Before KNOCH, CASTLE and SWYGERT, *Circuit Judges.*

CASTLE, *Circuit Judge.* Edward J. Brunenkant, plaintiff-appellant, brought this action in the District Court, pursuant to 42 U.S.C.A. § 405(g), to review a final decision[1] of the Secretary of Health, Education and Welfare denying the claims of plaintiff and his wife for old-age insurance benefits under the Social Security Act.[2] The District Court granted summary judgment for the defendant-appellee and the plaintiff appealed.

1 The final decision is a decision by the Appeals Council of the Social Security Administration affirming a decision made by a referee (hearing examiner) of the Administration.

2 Title II of the Social Security Act (42 U. S. C. A. §§ 401-425 (referred to herein as "Act".

Plaintiff and his wife applied for old-age insurance benefits on January 15, 1958. Denial of the applications led to the subsequent administrative proceeding and judicial review action which culminated in this appeal. Plaintiff had reached retirement age on December 21, 1957. Under the then applicable provisions of the Act, in order to qualify as fully insured for old-age insurance benefits, he was required to have either 13 quarters of coverage among the 27 quarters elapsing between January 1, 1951 and September 30, 1957 or at least 7 of the 11 quarters elapsing between January 1, 1955 and September 30, 1957. It is conceded that the limitation period of the Act (42 U.S.C.A. § 405(c)) makes uncontestable plaintiff's claim to 4 quarters of coverage during 1953 upon income he reported for that period as creditable self-employment income. Plaintiff claims that the record establishes that he received income creditable as self-employment income or as wages during the years 1955, 1956 and 1957 which for old-age insurance coverage purposes supplies the necessary additional quarters, or in itself constitutes the requisite quarters of coverage, for his qualification as fully insured.

We recently had occasion to point out (*Sherrick* v. *Ribicoff*, 7 Cir., 300 F. 2d 494, 495) that under the provisions of § 205 (g) of the Act (42 U.S.C.A. § 405(g)) the factual findings of the Secretary, if supported by substantial evidence, are conclusive and that this finalty attaches not only to the findings themselves but also to the inferences and conclusions drawn from the facts if a substantial basis for them appears in the record.

Thus the contested issue presented for our determination by plaintiff's appeal is whether the Secretary's findings and conclusions that the plaintiff did not in the years 1955, 1956 and 1957 receive income creditable for old-age insurance coverage purposes are supported by substantial evidence and based upon the application of correct legal criteria.

Plaintiff contends that his 1955-1957 income or earnings from futures trading on his own account as an "odd-lot- specialist" in wheat futures on the Chicago Board of Trade are creditable as self-employment income. He further contends that he received other 1955-1957 earnings from a corporation of which he was president which are creditable as wages or, in the alternative, that the 1956-57 portion of such earnings is self-employment income received for legal services rendered the corporation.

The basic facts are not in dispute. The record establishes that the plaintiff is a licensed attorney. For a number of years, including the 1955-1957 period, he was a member of the Chicago Board of Trade, a commodity exchange, and engaged in buying and selling of wheat futures as an odd-lot specialist. In addition he traded as a speculator in futures of other commodities. An odd-lot specialist is one who, in contrast to the usual futures trading in "round" lots of 5,000 bushels restricts himself to the buying and selling of smaller quantities of a particular commodity. A distinctive feature of an odd-lot specialist's transactions in futures is the ⅛ of a cent margin involved. Odd-lot futures are bought for ⅛ cent per bushel below, and sold for ⅛ cent per bushel above, the current market price.

Plaintiff's contention that his profits from his odd-lot specialist trading constitute creditable self-employment income was rejected by the final administrative decision of the Secretary affirmed by the District Court. We perceive no error in that ruling. Profits from futures trading are considered for income tax purposes as gains from the sale or exchange of capital assets. *Faroll* v. *Jarecki*, 7 Cir., 231 F. 2d 281, cert. den., 352 U.S. 830. Therefore, such profits are clearly within the express exclusion of § 211(a) (3) (A) of the Act (42 U.S.C.A. 411(a) (3) (A)), and are to be disregarded for the purposes of computing self-employment income under the Act. In *Faroll* we distinguished *Corn Products Refining Co.* v. *Com-*

missioner, 350 U.S. 46 as a case where such profits were held to constitute ordinary income and not capital gains because of the hedging aspect there involved *and* the fact that the future transactions were an integral part of the taxpayer's manufacturing business. In that case a manufacturer of corn products purchased corn futures in order to protect its manufacturing operations against a price increase in its principal raw material and to assure a ready supply for future manufacturing requirements without providing storage facilities. It took delivery of some of the corn according to its needs and sold the remainder at a profit. The futures transactions there involved afforded partial insurance against the principal risk of its manufacturing enterprise—a price rise in the raw material. The taxpayer's sales policy, selling its products for future delivery at a set price or at market price on the date of delivery, whichever was the lower, left it exceedingly vulnerable to rises in the price of corn.

Plaintiff's reliance upon *Corn Products* is misplaced. Plaintiff was not a manufacturer, processor or handler of the actual commodity but merely a trader in futures of the commodity who did not contemplate taking possession of the "actuals". Moreover, although plaintiff attempted to maintain a balance in his futures commitments, as nearly as market conditions would permit, the record does not disclose that his purchases and sales were ever perfectly matched. And to the extent that his futures commitments remained unmatched he took the full risks of price swings. In addition the illustrative daily trade records submitted by the plaintiff reflect the realities of the market. There was no matching of each purchase or sale at identical prices and his profit (or loss) consisted of both the ⅛ cent per bushel margin exacted for odd-lot transactions, a built-in capital gain in such transactions, and the price differential between the matched transactions. The fact that plaintiff chose contemporaneously to match most of his transactions (thereby taking only the risk of the daily short swings in the market), and run the risk of long-run price fluctuations on a

small part of his trading merely reveals plaintiff's conservative trading position. The limited degree of his speculation does not, for the purposes here concerned, either change the nature of his trading activities or qualify his profits therefrom as self-employment income rather than capital gains.

The evidence concerning receipt of wages by the plaintiff during the 1955-1957 period, except for certain entries in the records and tax returns of Commodity Investment Corporation, consists of plaintiff's testimony that in 1955 he was paid $3,576.00 in cash as salary by the corporation, and in 1956 and 1957 he was given notes of the corporation for $3,576.00 and $3,673.48, respectively, in payment of salary, which notes were exchanged for stock issued by the corporation in 1960 for their payment.

Commodity Investment Corporation was formed by the plaintiff, his wife, and his daughter, who comprised its board of directors. It was capitalized at $1,000 represented by 1,000 shares of common stock authorized and issued. Plaintiff, the corporation's president and treasurer, owned the controlling interest. The remaining stock was owned by plaintiff's wife, the corporation's secretary, and by his daughter, and his son. Neither the wife nor the daughter received any compensation for services as officer or director of the corporation. The corporation's address was that of plaintiff's residence; it had no telephone listing, nor did its name appear on any corporate registry other than that published by the state of its incorporation. The corporation's bank account carried a nominal balance of from $200.00 to $400.00.

The corporation had no income prior to 1955 at which time it commenced trading operations. Although its charter permitted of a broader range of activities the corporation's actual activity was limited to commodity trading on the Chicago Board of Trade where it availed itself of plaintiff's membership. Its primary "asset" was the privilege afforded by plaintiff's Board of Trade membership and its income was solely

the product of the use made of that membership in trading activities.

In 1955, the corporation's gross receipts were $4,500. Its balance sheet for that year discloses a net profit of $6.00 after deduction of $294.00 in expenses other than $4,200.00 listed as "salaries." In 1956 and 1957 the corporation sustained net operating losses of $3,974.84 and $2,671.03 according to its balance sheets and the plaintiff testified he was given notes for his salary. In 1958 the corporation decided to pay pay salaries only if it made money and provided that each officer was to receive a stated percentage of annual net earnings. In that year on gross receipts of $728.00 a net operating loss of $21.97 was sustained.

The administrative finding and conclusion that plaintiff's family corporation was utilized as a mere device to secure social security coverage through a personal activity of the plaintiff which was otherwise barred from such coverage finds substantial support in the record. The evidence considered as a whole, including the inferences which have a reasonable and substantial basis therein, support the conclusion that during the years 1955-1957 the sole function of the corporation was its utilization by the plaintiff as a device to create a sham employment relationship for the sole purpose of attempting to convert his non-creditable earnings from futures trading into creditable wages. The corporation was a family corporation under plaintiff's sole and complete control. Its sole income producing activity involved the use of his exchange membership. The regularity and validity of its organization does not serve to overcome the fact that its "corporate shell" was diverted to the purpose of serving as a channel through which plaintiff's membership on the exchange might serve to produce "wages" creditable to him for social security purposes. *Cf. Higgins v. Smith*, 308 U.S. 473, 476-478; *Hoggatt v. Folsom*, E. D. Pa., 160 F. Supp. 490, affirmed 253 F. 2d 680 (C.A. 3). Although the corporation was organized in 1953 it was not until

1955 that it commenced trading activities. Early in 1955 plaintiff had learned that his gains from futures trading on his own account, because of the reversal of an earlier Bureau of Internal Revenue ruling, would no longer be regarded as creditable self-employment income. And, it was not until that same year that he was voted a salary as president and treasurer of the corporation.

Moreover, although the corporation remitted the social security taxes due on the salary plaintiff testified he was paid, he presented no evidence to corroborate the receipt of the $3,576.00 cash salary payment for 1955. His testimony as to the nominal bank balance of the corporation appears inconsistent with such a payment. The 1956 salary note was not produced. The evidence of the 1957 payments are the notes which in turn were redeemed in 1960 by the issuance of stock which, in the light of the evidence concerning the corporation's financial structure and net operating losses, would appear to be worthless.

Nor are we persuaded by plaintiff's alternative contention that the 1956-1957 portion of his earnings from the corporation was self-employment income attributable to services rendered the corporation as a lawyer. The contention is wholly inconsistent with the documentary evidence presented and relied upon by the plaintiff—material of the plaintiff's own making—to establish his receipt of "wages" from the corporation and it is in direct conflict with the declarations made in his application for benefits that his self-employment earnings as a lawyer for each of those years was less than $400.00. Plaintiff points to a 1953 entry in the corporate minutes that plaintiff was to be paid for legal services performed "in his individual capacity as a practicing lawyer" in connection with the qualifying and underwriting of an issue of $1,000,000.00 of cumulative prefered stock authorized by the charter. But the compensation so authorized appears to bear no relationship to the $4,200.00 salary the directors resolved in each of the years 1955, 1956 and 1957 to pay the plaintiff "as President and Treasurer" of

the corporation. The payments plaintiff claims to have received were in the latter amount (less tax deductions). The amount was also the maximum annual wages creditable for social security purposes.

The judgment order of the District Court is affirmed.

AFFIRMED.

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In the Supreme Court of the United States

OCTOBER TERM, 1962

No. 970

EDWARD J. BRUNENKANT, PETITIONER

v.

ANTHONY J. CELEBREZZE, SECRETARY OF HEALTH, EDUCATION AND WELFARE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The district court, in granting the Secretary's motion for summary judgment, wrote no opinion. The opinion of the court of appeals, affirming the district court's order, is reported at 310 F. 2d 355 (Pet. 16–23).

JURISDICTION

The judgment of the court of appeals was entered on October 31, 1962, and a petition for rehearing was denied on January 2, 1963. The petition for a writ of certiorari was filed on April 1, 1963. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether both courts below correctly held that there was substantial evidence in the administrative record to support the determination of the Secretary of Health, Education and Welfare that, during the period 1955 through 1957, petitioner received neither "self-employment income" nor "wages" within the meaning of Sections 211 and 209 of the Social Security Act.

STATUTE INVOLVED

The relevant provisions of the Social Security Act are, in pertinent part, the following:

Section 205(g), 53 Stat. 1368, as amended, 42 U.S.C. 405(g):

> * * * The findings of the Secretary as to any fact, if supported by substantial evidence, shall be conclusive * * *.

Section 209, 49 Stat. 625, as amended, 64 Stat. 492, 42 U.S.C. 409:

> For the purposes of this subchapter, the term "wages" means * * * remuneration paid after 1950 for employment, including the cash value of all remuneration paid in any medium other than cash * * *.

Section 211(a), 64 Stat. 502, as amended, 42 U.S.C. 411(a):

> (a) The term "net earnings from self-employment" means the gross income, as computed under chapter 1 of Title 26, derived by an individual from any trade or business carried on by such individual * * *; except that in computing such gross income * * *

* * * * *

(3) There shall be excluded any gain or loss (A) which is considered under chapter 1 of Title 26 as gain or loss from the sale or exchange of a capital asset * * *.

STATEMENT

In this action, commenced under Section 205(g) of the Social Security Act, 53 Stat. 1368, 42 U.S.C. 405(g), petitioner seeks to overturn the decision of the Secretary of Health, Education and Welfare that he was not entitled to social security benefits. The Secretary's decision was based on the finding that, during the period 1955 through 1957, petitioner had received neither "self-employment income" nor "wages" within the meaning of Sections 211 and 209, respectively, of the Social Security Act, *supra*, pp. 2–3, and thus lacked sufficient "quarters of coverage" [1] to qualify as "fully insured" [2] for old-age-insurance benefits.

Petitioner is licensed to practice law in Illinois and Ohio. In addition, he has been a member of the Chicago Board of Trade, a commodities exchange, since 1939. As such, he engaged in the buying and selling of commodity futures. During the period in question he acted as an odd-lot specialist [3] in wheat futures and as a speculator in futures of other com-

[1] As defined by Section 213(a), 64 Stat. 504, as amended, 42 U.S.C. 413(a).

[2] As defined by Section 214(a), 64 Stat. 505, as amended, 42 U.S.C. 414(a).

[3] In contrast to the usual futures trading in "round" lots (*i.e.*, 5,000-bushel lots), an odd-lot specialist trades in the more limited market for "job" or "odd" lots (*i.e.*, 1,000-bushel lots).

modities. Only his odd-lot activities are relevant here.

Prior to 1955, petitioner's odd-lot futures trading was conducted strictly in his own behalf; that is, he traded not as a broker but on his own account with his own funds. During this period he reported his earnings from such trading as capital gains for income tax purposes, but reported the same earnings for purposes of the Social Security Act as covered "self-employment income." Upon learning that earnings from futures trading, which are capital gains for income tax purposes, were within the express exclusion from coverage contained in Section 211(a)(3) of the Act, *supra*, pp. 2–3, petitioner ceased reporting such income, for Social Security Act purposes, as creditable earnings from self-employment.[4] Thereafter, during the period presently in controversy (1955 through 1957), petitioner continued to report his profits from odd-lot trading as capital gains for income tax purposes.

From 1955 through 1957, in addition to continuing odd-lot trading in his own behalf, petitioner pur-

[4] Petitioner's application for benefits claimed coverage for "self-employment income" from personal odd-lot futures trading during 1953 and 1954. The Bureau of Old-Age and Survivors Insurance of the Social Security Administration held itself barred by the Act's limitation period—contained in Section 205(c), 53 Stat. 1368, as amended, 42 U.S.C. 405(c)—from attacking the claimed 1953 earnings (and, thus, petitioner was accorded 4 quarters of coverage). As to the claimed 1954 earnings, however, the Bureau held them not covered. Petitioner did not attack this determination in the district court or the court of appeals, nor does he raise the question in the present petition.

ported to engage in identical trading in behalf of his family corporation, Commodity Investment Corporation. Although organized in 1953,[5] the corporation began functioning only in 1955, at the same time that petitioner ceased reporting the earnings from his odd-lot trading as "self-employment income" for Social Security Act purposes. The corporation's only activity was petitioner's odd-lot trading on its behalf, trading identical to that previously and concurrently engaged in by petitioner on his own account. The "primary asset" of the corporation was having petitioner on the Board of Trade, a membership that was personal and could not be transferred to the corporation, and corporate earnings were solely the product of this "asset."

During the years 1955 through 1957, petitioner was purportedly paid "wages" for his activity on behalf of the corporation. In 1955, the corporation purportedly earned $4,500, of which petitioner said he was paid $4,200 (the maximum annual wages then creditable under the Act); petitioner could produce no corroboration of this assertion, either in the form of cancelled checks or personal bank deposit state-

[5] The corporation was formed in Illinois by petitioner, his wife and their daughter in 1953, and was capitalized at $1,000. The three incorporators comprised the corporation's board of directors. In addition, petitioner was made its president and registered agent and petitioner's wife its secretary. Petitioner held a controlling interest in the outstanding stock of the corporation, and his wife and children held the balance. The corporation's address was that of petitioner's residence; it had no telephone listing, nor did its name appear on any corporate registry other than that published by the State of Illinois; at all times its bank account contained a nominal balance of from $200 to $400.

ments. In 1956, the corporation purportedly earned only $356.16, yet petitioner was allegedly paid $4,200. And in 1957 the corporation purportedly earned only $1,827.07, yet again petitioner was allegedly paid $4,200. In each of the last two years, "payment" was made in the form of promissory notes, signed by petitioner as president, which were not negotiable in form, and were never, in fact, paid.[6] In 1958, the year in which he reached retirement age and thus could have no more creditable earnings, the board of directors altered its compensation policy so as to pay salaries only in the event of profitable operation.

On the basis of the foregoing activity, petitioner filed an application for old-age insurance benefits.[7] While his application was based on other claims to coverage,[8] the two that remain in controversy both

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[6] After rejection of his claims by the Social Security Administration referee (now hearing examiner), and prior to review by the Appeals Council, the corporation's board of directors met and purported to redeem these notes by issuance of stock to petitioner. As noted below, note 14, *infra*, this transaction was ignored by the court below as completely lacking substance.

[7] Petitioner's wife also filed an application for wife's benefits. Her entitlement to such benefits is, of course, dependent upon petitioner's status. She joined neither the appeal to the court of appeals nor the present petition.

[8] Petitioner originally claimed "self-employment income" from futures trading during 1953 and 1954. See note 4, *supra*. In addition, petitioner claimed for the first time before the referee that the 1956–1957 portion of the claimed "wages" were "alternatively" creditable as "self-employment income" for legal services rendered to the corporation. Both the Secretary and the court of appeals rejected this so-called alternative claim as lacking evidentiary support and, in fact, inconsistent with petitioner's claim to "wages". (Pet. 22–23). Petitioner no longer contests this determination.

relate to the period 1955 through 1957: (1) that his earnings from odd-lot futures trading on his own account, although reported as capital gains for income tax purposes, qualify as "self-employment income" for Social Security Act purposes; and (2) that the salary he purportedly received from Commodity Investment Corporation constitutes creditable "wages" under the Act. The Secretary denied both claims.

With respect to petitioner's claim to coverage for earnings from personal odd-lot trading, the Secretary held that since commodity futures are universally regarded as capital assets, and since gains from the sale or exchange of capital assets are expressly excluded from Social Security coverage by Section 211(a)(3) of the Act, *supra*, pp. 2–3, petitioner had received no creditable "self-employment income" during the period in question. The Secretary expressly rejected petitioner's factual claim that his odd-lot trading was not speculative, because not dependent upon market fluctuations, and therefore constituted an exception to the above rule. On the basis of petitioner's own description of his practice, the Secretary found that while petitioner succeeded in partially reducing the risk of price fluctuations by matching a majority of his purchases or sales with corresponding sales or purchases at similar prices, the broad range of his trading remained fully subject to market fluctuations and was therefore speculative, albeit not to the fullest extent possible.

With respect to petitioner's claim that he received creditable "wages" from his family corporation, the

Secretary held that the corporate arrangement was to be disregarded as a mere sham or device employed by petitioner to circumvent the exclusion from Social Security Act coverage of earnings from futures trading (capital gains), and that, in any event, petitioner had failed to prove that the claimed salary had, in fact, been paid.

On review,[9] the district court granted the Secretary's motion for summary judgment without opinion. The court of appeals affirmed, holding that the Secretary's decision was fully supported by substantial evidence (Pet. 16–23). With respect to petitioner's claim to "self-employment income," the court confirmed the Secretary's finding that petitioner's trading was indeed speculative, and thus constituted no exception to the usual rule barring such earnings from coverage (Pet. 18–20). With respect to petitioner's claim to "wages," the court found substantial record support for the Secretary's findings (1) that the corporate arrangement was a mere device, lacking in substance, and utilized to convert non-creditable earnings into creditable "wages," and (2) that, in any event, the claimed salary had never been paid (Pet. 20–22).

ARGUMENT

Determination of the underlying issues turns essentially on the particular facts of petitioner's case. Since the overall question presented is thus a factual

[9] The Appeals Council originally declined to review the referee's determination. The district court, on its own motion, remanded the case for further hearing. The Appeals Council then took additional evidence and affirmed the referee's decision. The case was then again brought to the district court.

one, and since the Secretary's determination was clearly supported by substantial evidence, both courts below correctly held that determination binding. Therefore, there is plainly no occasion for further review.

1. Section 211(a)(3) of the Social Security Act, *supra*, pp. 2–3, expressly provides that capital gains are excluded from Social Security Act coverage. Commodity futures are universally regarded as capital assets,[10] even where the trading of such futures constitutes the taxpayer's full-time business,[11] and the profits from such trading constitute capital gains. *Faroll* v. *Jarecki*, 231 F. 2d 281 (C.A. 7), certiorari denied, 352 U.S. 830.

On the basis of the foregoing well-established principles, the Secretary determined that petitioner's earnings from odd-lot futures trading constituted capital gains, rejecting his claim that they did not qualify as such because they were not speculative. The court of appeals found this determination amply supported by the administrative record, observing (Pet. 19–20):

> The fact that [petitioner] chose contemporaneously to match most of his transactions (thereby taking only the risk of the daily short

[10] *E.g., Estate of Dorothy Makransky*, 5 T.C. 397, affirmed *per curiam*, 154 F. 2d 59 (C.A. 3); *Modesto Dry Yard, Inc.*, 14 T.C. 374; *Tennessee Egg Co.*, 47 B.T.A. 558.

[11] *Craig M. Smith*, 33 T.C. 465, 485. Thus, petitioner cannot import a third question into this case, one not decided by the court of appeals, by asserting (Pet. 13–14) that his odd-lot trading was his "trade" or "business," that his futures contracts were his "inventory" and that such inventory property is recognized as non-capital in nature.

> swings in the market), and run the risk of long-run price fluctuations on a small part of his trading merely reveals [petitioner's] conservative trading position. The limited degree of his speculation does not, for the purposes here concerned, either change the nature of his trading activities or qualify his profits therefrom as self-employment income rather than capital gains.

Petitioner has demonstrated no error in these conclusions.[12]

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[12] Petitioner asserts here, as he did in the court of appeals, that his matching practice constitutes "hedging" within this Court's decision in *Corn Products Refining Co.* v. *Commissioner*, 350 U.S. 46, and that his trading is thus excepted from the usual capital transaction characterization (Pet. 9–11). However, the *Corn Products* decision, and the cases which build upon it, demonstrate that the "hedging" exception to the capital transaction result inures only to the benefit of a producer, manufacturer or processor of a commodity who trades in the futures of that commodity in order to control its cost-of-goods-sold by stabilizing the cost of its inventory, and that one who merely trades in futures cannot "hedge" in this special sense of the term. See, *e.g.*, *Farrell* v. *Jarecki*, *supra*, 231 F. 2d 281 (C.A. 7), certiorari denied, 352 U.S. 830; *Flora* v. *United States*, 142 F. Supp. 602, 605–606 (D. Wyo.), dismissed on other grounds, 246 F. 2d 929 (C.A. 10), affirmed, 357 U.S. 63, 362 U.S. 145; *Steanoff Vegetable Oil Corp.*, 27 T.C. 1056, 1067–1068, reversed on other grounds, 251 F. 2d 764 (C.A. 7). In view of these requirements the court of appeals properly rejected petitioner's assertions that his odd-lot trading constituted hedging (Pet. 19): "[Petitioner's] reliance upon *Corn Products* is misplaced. [He] was not a manufacturer, processor or handler of the actual commodity but merely a trader in futures of the commodity who did not contemplate taking possession of the 'actuals.'" Petitioner's assertion that this holding is in conflict with the *Corn Products* rule is plainly without merit.

2. With respect to petitioner's claim to "wages" based upon the putative employment by his family corporation, the Secretary held that the corporation could be disregarded as a mere sham or device employed to circumvent the exclusion from coverage of petitioner's earnings from futures trading on his own account, and that, in any event, the claim to "wages" must be rejected since petitioner failed to prove the actual receipt of the alleged salary. The court of appeals sustained this determination as supported by substantial evidence (Pet. 20-22).

The petition does not attack the substantiality of the evidence supporting the finding that petitioner's family corporation was a sham for Social Security Act purposes. Rather, petitioner relies on the assertion that such an inquiry is beyond the power of the Secretary and urges that the decision below conflicts with *Stark* v. *Flemming*, 283 F. 2d 410 (C.A. 9).

There is no conflict with the *Stark* case,[11] but even if there were, this case would be an inappropriate

[11] In *Stark*, the Ninth Circuit held that where there has been "proper adherence to the normal corporate routines * * * it is difficult to understand how the corporate arrangement would not have to be respected by others than the Secretary. And we think he must respect it, too" (283 F. 2d at 410). This holding plainly implies that the Secretary can inquire whether, following incorporation, the business was conducted in conformity with "the normal corporate routines," and upon finding that it has not, disregard it as a separate legal entity for Social Security Act purposes, which is, of course, precisely what he did here.

Petitioner also alleges conflict in another Ninth Circuit case, *Flemming* v. *Lindgren*, 275 F. 2d 596. But if *Lindgren* has any bearing upon this question it demonstrates that there is no

one for its resolution. For no matter what might be concluded with respect to the Secretary's power to "pierce the corporate veil" for purposes of determining the true nature of petitioner's so-called "wages" for Social Security Act purposes, the Secretary found that petitioner had not actually received the putative salary from the corporation. With respect to the alleged 1955 cash salary, the record contains only petitioner's uncorroborated assertion. And with respect to 1956 and 1957, plaintiff received promissory notes, which the Secretary observed were non-negotiable and, in fact, unpaid.[11] In such circumstances the court of appeals had little difficulty in concluding that the Secretary's finding was fully supported by the administrative record and thus binding (Pet. 22). Petitioner has not demonstrated even arguable error in this finding.

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conflict here, for there the Ninth Circuit stated that the Secretary "must be permitted to look through form to substance," and where a "rather shallow corporate device" is employed, he is "entitled to take not one, but several long looks at it" (275 F. 2d at 597).

[11] As noted above, note 6, *supra*, an attempt was made, in the interim between the referee's and Appeals Council's decisions, to give substance to these notes by issuance of corporate stock in purported redemption. The Secretary, noting its timing, held that this transaction was without substance, since the issued stock was itself worthless. The court of appeals, in affirming this finding, held that "in light of the evidence concerning the corporation's financial structure and net operating losses," the stock "would appear to be worthless" (Pet. 22).

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for a writ of certiorari should be denied.

ARCHIBALD COX,
Solicitor General.

JOHN W. DOUGLAS,
Assistant Attorney General.

MORTON HOLLANDER,
STEPHEN B. SWARTZ,
Attorneys.

MAY 1963.

U. S. GOVERNMENT PRINTING OFFICE 1963